

Internal Revenue Service
Director, Exempt Organizations

Department of the Treasury
P.O. Box 2508 – EP/EO
Cincinnati, OH 45201

Date: NOV 19 2001

Employer Identification Number:
[REDACTED]

Person to Contact – I.D. Number:
[REDACTED] - [REDACTED]

Telephone Number:
[REDACTED] / [REDACTED]

FAX
[REDACTED]

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(5) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth on Enclosure I.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Code. However, we have concluded that you do not qualify under another subsection.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1041 if you are a Trust, or Form 1120 if you are a corporation or an unincorporated association.

If you are in agreement with our proposed denial, please sign and return one copy of the enclosed Form 6018, Consent to Proposed Adverse Action.

You have the right to protest this proposed determination if you believe it is incorrect. To protest, you should submit a written appeal giving the facts, law and other information to support your position as explained in the enclosed Publication 892, "Exempt Organizations Appeal Procedures for Unagreed Issues." The appeal must be submitted within 30 days from the date of this letter and must be signed by one of your principal officers. You may request a hearing with a member of the office of the Regional Director of Appeals when you file your appeal. If a hearing is requested, you will be contacted to arrange a date for it. The hearing may be held at the Regional Office or, if you request, at any mutually convenient District Office. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements as set forth in Section 601.512 of the Statement of Procedural Rules. See Treasury Department Circular 0.

[REDACTED]

If we do not hear from you within the time specified, this will become our final determination.

Sincerely,

Steven T. Miller

Steven T. Miller
Director, Exempt Organizations

Enclosures:
Enclosure
Form 6018
Publication 892

Enclosure I

FACTS

Per the application submitted you indicate that your primary activity is to provide a "regional marketplace for high quality locally produced agricultural and horticultural products." Another substantial activity of the organization is to the patronage of the marketplace. You indicate that the you were organized for two objectives a) "To provide an outlet for locally grown produce and other items made by local residents" and b) "To provide a convenient location for residents to purchase home-grown or home-made items."

Your Articles of Incorporation state the organizations' purpose as:

"To promote the social welfare by providing and managing facilities for use by growers, producers and makers in the public display and sale of their farm and garden products, handcrafts, and home baked goods and canned goods and other food items, thereby to encourage the supply of such articles and thus to contribute to the betterment of community relationships and its economic health."

Your By-laws similarly indicate the purpose of your organization is to organize a community volunteer group to promote the products of farmers, bakers and crafts people in an effort to encourage "residents and visitors to appreciate and purchase locally handcrafted articles and locally grown produce."

Per subsequent response submitted (correspondence dated [REDACTED]) you indicated that the organization's focus had shifted to education and the improvement of products. You indicated that the "market consisted of only [REDACTED]% of all activities with [REDACTED]% of time being devoted to the betterment of conditions of farmers and growers and [REDACTED]% to teaching about progressive innovations and conservation practices." No supporting information was provided in regards to how your activities improved the conditions of farmers or growers other than providing them a place to market their goods.

This information also directly contradicts your application dated [REDACTED] as well as your subsequent response of [REDACTED]. Per your application you indicate that [REDACTED]% of your time is spent as a "regional marketplace for high quality locally produced agricultural and horticultural products." You further indicate that [REDACTED]% is spent toward promoting patronage to the market. Per your correspondence dated [REDACTED] you indicated "our board simply organizes parking, coordinates social feature program, advertises and provides organizational management."

Per our correspondence and conversations with [REDACTED] subsequent information documenting the organizations' agricultural, educational and cultural activities was requested. Per the information submitted you have indicated "vendors are educational and agricultural/cultural." Also, you have emphasized that your "featured" vendor program is "[REDACTED]% education and/or farm/agricultural/horticultural promotional." You have also indicated that you invite county extension agents who provide lectures/displays regarding various topics. The information submitted indicates that no more than [REDACTED] slots a week are available for these programs.

Information has been requested regarding the educational, cultural or agricultural activities of the other vendors who participate in your marketplace. Per your response dated [REDACTED] you indicate that vendors provide substantial educational activities. You state: "A good vendor (and we have many good vendors) realizes that the explanation of the product was grown/made is part of a good sale." This statement would appear to be an acknowledgement that the organization's focus is to provide individuals the opportunity to sell their products. While some of the vendors who participate in your market may have some educational aspects to their presentations this would not appear to be the primary focus of the market. There

no supporting evidence provided to indicate how vendors having an independent economic interest and having no obligation to put educational or cultural purposes ahead of profit making objectives, will be operated in furtherance of agricultural, educational or cultural purposes. No information was provided to indicate how you further agricultural pursuits other than to provide a second income to vendors.

Per the application submitted [REDACTED] you indicate that the sources of financing the organization come from vendor's fees, contributions to a permanent site project, and the sales of merchandise (T-shirts, pens, etc.) Per your application submitted [REDACTED] you indicate your sources of financial support come from vendor's fees and investment income. Per the budgets submitted there is no indication of gifts, grants or contributions being received.

Information submitted for the most recent years completed ([REDACTED] and [REDACTED]), indicates that you have [REDACTED] and [REDACTED] spots available for vendors. In [REDACTED] [REDACTED] spots per weekend were reserved for "featured" vendors and [REDACTED] spots in [REDACTED].

"Featured" vendors are invited to participate at the market to provide educational information to patrons. No rental fee is charged to these vendors. Past "featured" vendors have included 4-H demonstrations, as well as demonstrations regarding the making of certain items or crafts and the display of various hobbies (raising butterflies or exotic animals.)

Rental space for vendors in [REDACTED] and [REDACTED] were \$[REDACTED]/day if the vendor participated more than half the season ([REDACTED] weeks) and \$[REDACTED]/day if the vendor participated less than half the season ([REDACTED] weeks.)

Even conservatively estimating the number of vendor participants, it would appear that substantially all of your income is derived from person's for whom space is provided. Disbursements per the budgets submitted are for the operations of the markets activities, advertising and contract services.

The minutes to meetings provided substantiate the predominate commercial purpose. Per the minutes, as well as the submitted budgets, a significant portion of your budget is allocated toward advertising with any remainder to be used for the purchase of a permanent site or facility for the market.

Your principle activity is to make space available to farmers, bakers and craftspeople, who wish to market their products to consumers. Making sales space available to members in exchange for membership dues or for rental fees for the individual marketing and sale of their personal goods produced by them is a commercial activity unto itself carried on by you.

LAW

Section 501(c)(5) of the Code provides for the exemption from Federal income tax of agricultural or horticultural organizations.

Section 1.501(c)(5)-1 of the Income Tax Regulations provides that the organizations contemplated by section 501(c)(5) of the Code as entitled to exemption from income taxation are those which (1) have no net earnings inuring to the benefit of any member, and (2) have as their objects the betterment of the conditions of those engaged in such pursuits, the improvement of the grade of their products, and the development of a higher degree of efficiency in their respective occupations.

Section 511 of the Code imposes a tax on unrelated business taxable income of organizations exempt from Federal income tax under section 501(a) and 501(c)(3).

Section 512(a)(1) of the Code defines "unrelated business taxable income" as the gross income derived by an organization from any unrelated trade or business regularly carried on by it, less allowable deductions.

Section 513(a) of the Code defines the term "unrelated trade or business" as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of profits derived) to the exercise or performance by such organization of the purposes or function constituting the basis for its exemption under 501.

Regulations 1.513-1(c)(1) indicates in determining whether a trade or business is "regularly carried on" within the meaning of IRC 512, regard must be had to the frequency and continuity with which the activities are conducted and the manner in which they are pursued. This requirement must be applied in light of the purpose of the unrelated business income tax to place exempt organizations business activities upon the same tax basis as the nonexempt business endeavors with which they compete. Hence, for example, specific business activities will ordinarily be deemed "regularly carried on" if they manifest a frequency and continuity, and are pursued in a manner generally similar to comparable commercial activities of nonexempt organizations.

Regulations 1.513-1(c)(2) states where income producing activities are of the kind normally conducted by nonexempt commercial organizations on a year round basis, the conduct of such activities over a shorter period of time, such as a few weeks, would not constitute the regular carrying on of a trade or business. Where income producing activities are of a kind normally undertaken by nonexempt commercial organizations only on a seasonal basis, the conduct of such activities by an exempt organization during a significant portion of the season ordinarily constitutes the conduct of a trade or business.

Regulations 1.513-1(c)(2) offers examples of the principles given above.

- (a) The operation of a commercial parking lot on Saturday of each week year round would be the regular conduct of trade or business.
- (b) The operation of a track for horse racing for several weeks of a year would be considered the regular conduct of trade or business because it is usual to carry on such trade or business only during a particular season.

Section 501(c)(4) of the Code provides for the exemption from Federal income tax of civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare.

Section 1.501(c)(4)-1 of the regulations provides that an organization is not operated primarily for the promotion of social welfare if its primary activity is carrying on a business with the general public in a manner similar to organizations which are operated for profit.

Section 1.501(c)(4)-1(a)(2) of the Income Tax Regulations provides that an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. An organization coming within the scope of this section is one which is operated primarily to bring about civic betterment's and social improvements.

Section 1.501(c)(3)-1(c)(1) of the Regulations states that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the Regulations states that an organization is not operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. It must not be operated for the benefit of designated individuals or the persons who created it.

APPLICATION OF LAW

Revenue Ruling 66-105, 1966-1 CB 145

The organization was formed as a nonprofit corporation to carry out a livestock improvement program and to sponsor and promote sales of livestock for its members who are owners or operators of farms. The organization's principal activity is marketing livestock as agent for its members at auctions held throughout the year. It furnishes the labor, advertising, bookkeeping services, and physical facilities required for the auctions.

The principal purpose of the organization is to act as a sales agent for its members. Therefore, the organization does not meet the requirements of section 1.501(c)(5)-1 of the regulations and is not exempt under section 501(c)(5) of the Code.

Revenue Ruling 69-51, 1969-1 CB 159

An organization formed to promote the betterment of conditions of breeders of Angus cattle and to improve the breed generally. Its activities consist of encouraging junior breeder programs by conducting shows, awarding trophies, and cooperating with 4-H and Future Farmers programs; conducting an educational program in conjunction with its annual meeting; disseminating general information concerning Angus breeding through an annual directory and a monthly newsletter; cooperating with other agencies interested in promoting agriculture; and sponsoring shows and displays of prize cattle. As one of its lesser activities the organization regularly sells cattle for its members on a commission basis.

In this instance the sale of cattle constitute trade or business that is regularly carried on. The sale of members' cattle for a commission is not an activity coming within the ambit of section 501(c)(5) of the Code. The sale itself neither promotes the betterment of conditions of the cattle breeders nor improves the breed generally but is carried on for the convenience of members and the production of income. Furthermore, the sale is an activity having no casual relationship to the performance of the organization's exempt purpose and it does not contribute importantly to the accomplishment of that purpose.

Revenue Ruling 74-195, 1974-1 CB 135

A nonprofit organization formed to manage, graze, and sell its members' cattle is providing a direct business service to its members and does not qualify for exemption as an agricultural organization.

The cooperative management, grazing, and sale of members' cattle does not of itself better the conditions of those engaged in agricultural pursuits, improve the grade of their products, or develop a higher degree of efficiency in their operations within the meaning of the cited sections of the Code and regulations. The principal purpose of the organization is to provide a direct business service for its members' economic benefit.

Revenue Ruling 77-153, 1977-1 CB 147

The corporation's principal activity is the operation and leasing of this facility to local members of the national association. Each farmer using the facility pays a fee to the corporation based upon the weight and/or kind of livestock being marketed. This fee is set at a level that will pay operating costs as well as the monthly payments on indebtedness incurred in acquiring the land and constructing the facility. Once the indebtedness is paid, the fee will be reduced to cover only operating costs.

The operation and leasing of a facility for collecting, weighing, sorting, grading, and shipping of livestock, the organization's principal activity, is the providing of a business service to those members who make use of the national association's collective bargaining program. This service merely relieves the members of the organization of work they would either have to perform themselves or have performed for them. Such activity does not serve an exempt purpose of an agricultural organization under section 1.501(c)(5)-1 of the regulations.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279 (1945), the Court ruled that an organization which engaged in some educational activity but pursued non-profit goals outside the scope of the statute was not exempt under IRC section 501(c)(3).

An organization is not operated exclusively for charitable purposes if it has a single non-exempt purpose that is substantial in nature. This is true regardless of the number or importance of the organizations exempt purpose.

CONCLUSION

Based upon the information submitted and the manner in which you conduct your activities, it is clear that the organization's controlling purpose is to benefit individual members economically and only incidentally to further the larger public welfare or to better the conditions of those engaged in agricultural pursuits. It would appear clear that your purpose is to provide a direct business service for the convenience of your vendors and for their economic benefit.

The operation of a facility to enable individuals the opportunity to sell products to the general public does not in itself better the conditions of those engaged in agricultural pursuits, better the grade of their products, or develop a higher degree of efficiency in their operations within the cited regulations.

The fact that these services are being provided at minimal charge to vendors, enough to cover expenses and provide a surplus for a permanent facility, does not change the business purpose of the activity.

Your are similar to that of one described in Revenue Ruling 66-105, in that both organizations sponsor and market products for its members. Even though you are not acting as a sales agent for vendors, you are furnishing services and facilities for the convenience of vendors to market and sell their products. Revenue Ruling 74-195 is similar in that it indicates that by providing a direct business service for members economic benefit the organization is not furthering the purposes provided under the Code and regulations.

Similarly, Revenue Ruling 69-51 establishes that the sale of cattle constitute a trade or business that is regularly carried on. The sale itself neither promotes the betterment of conditions of the cattle breeders nor improves the breed generally but is carried on for the convenience of members and the production of income.

Revenue Ruling 77-153 concluded that an organization that owned and operated a livestock facility and leased it to local members did not qualify for exemption under section 501(c)(5) of the Code. This was based on the conclusion that the operation of a facility for collecting, weighing, sorting, grading and shipping of livestock, the organization's principal activity, was providing a business service. You are similar to the one described in Revenue Ruling 77-153, in that you are merely relieving vendors of work they would either have to perform themselves or have performed for them. Such activity does not serve an exempt purpose of an agricultural organization under section 501(c)(5) of the Code.

Your principle activity is to provide a marketplace for farmers, bakers and craftspeople, who wish to market their products to consumers. This is not an activity that falls within the meaning of section 501(c)(5) of the Code. Per the previous precedent cited it has been well established that an organization whose principle purpose is to provide a direct business service for its members economic benefit is not operating under the auspices of section 501(c)(5). Your controlling purpose is to benefit vendors economically and only incidentally to further larger educational, cultural or agricultural purposes. Your educational program (featured vendors) is insubstantial compared to your activities as a whole.

The concept of social welfare includes the provision of benefits to the community at large. Even though there may be some public benefit, your organization serves the private interests of the vendors by encouraging the public to patronize your market and purchase their products and furthering their individual economic interests, the organization is not operated primarily for social welfare purposes. Making sales space available to members in exchange for membership dues or for rental fees for the individual marketing and sale of their personal goods produced by them is a commercial activity unto itself carried on by your organization. Accordingly, the organization does not qualify for exemption under section 501(c)(4) of the Code.

As discussed in Better Business Bureau of Washington, D.C., Inc. v. United States, an organization which engages in some educational activity but pursued non-profit goals outside the scope of the statute was not exempt under section 501(c)(3) of the Code. An organization is not operated exclusively for charitable purposes if it has a single non-exempt purpose that is substantial in nature. This is true regardless of the number or importance of the organizations exempt purpose.

Accordingly, we conclude that you do not qualify for recognition of exemption under sections 501(c)(5), 501(c)(4) or 501(c)(3) of the Internal Revenue Code. Based on the information submitted, exempt status will not be recognized under any related paragraph of section 501(c).